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PUBLIC UTILITIES COMMISSION

BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF HAWAII

In the Matter of the PUBLIC UTILITIES COMMISSION Instituting a Proceeding to Investigate the Implementation Of Feed-in Tariffs.	)	DOCKET NO. 2008-0273

RESPONSE TO THRESHOLD ISSUES (LEGAL) IN APPENDIX C

OF THE NATIONAL REGULATORY RESEARCH INSTITUTE SCOPING PAPER

BY

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DOING BUSINESS AS FIRST WIND HAWAII

and

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HAWAII HOLDINGS, LLC,
DOING BUSINESS AS FIRST WIND HAWAII

TO THE HONORABLE PUBLIC UTILITIES COMMISSION OF THE STATE OF HAWAII:

HAWAII HOLDINGS, LLC, doing business as First Wind Hawaii, a Delaware limited liability company ("First Wind"), respectfully submits its preliminary responses set forth below to the Threshold Issues (Legal) in Appendix C of the National Regulatory Research Institute ("NRRI") scoping paper entitled *Feed-in Tariffs: Best Design Focusing Hawaii's Investigation* ("Scoping Paper"). The Commission, by its letter, dated December 11, 2008, to the parties in this docket directed them to respond to such Threshold Issues (Legal). First Wind submits its preliminary responses below for the Commission's consideration and use in its deliberations on these and related issues, but since this docket is in its initial stages, respectfully reserves its right to further elaborate its responses in future submissions in this docket as may be appropriate.

Threshold Issues (Legal)

1. If the price associated with a feed-in tariff exceeds the utility's avoided cost, then by definition the utility's customers will incur higher costs than they would in the absence of the feed-in tariff. Please comment on the legal implications of this result. For example:

   a) Is this result permissible under current Hawaii statutes?

RESPONSE:

This question is specifically limited to current Hawaii statutes.

This question has two aspects: (1) What are the legal implications under the Hawaii statutes of feed-in tariff ("FIT") rates that exceed the electric utility's avoided costs *at the time such energy is purchased by the utility*? (2) What are the legal implications under the Hawaii statutes if, because of the higher FIT rates, the rates proposed to be charged by the utility to its customers are higher than they would have been if the utility had not been required to purchase energy under the FIT? Each of these is briefly discussed below.

First, HRS § 269-27.2 provides for the purchase by electric utilities of electric energy generated by producers from nonfossil fuels. HRS § 269-27.2(c) specifically provides that the rate for purchase by a utility of such nonfossil fuel generated electric energy shall just and reasonable, shall not be more than one hundred percent of the cost avoided by the utility when it purchases such electric energy rather than produces such energy, and shall have no, or a significantly reduced, linkage to the price of fossil fuels. This rate for purchase shall be as agreed upon by the utility and the supplier and approved by the Commission, or if the parties fail to agree, then as prescribed by the Commission (i.e., just and reasonable, not more than 100% of the utility's avoided cost, and de-linked from fossil fuel prices). As a result, even if the utility and a nonfossil fuel producer agree to a rate for purchase that exceeds this limitation, the Commission, under this statute, may not approve such an rate for purchase.

The assumption underlying Question 1.a) is that the supplier of energy to the utility under the FIT will be a nonfossil fuel producer. Hence, HRS § 269-27.2(c) would impose a ceiling of 100% of the utility's avoided cost. However, this leaves open the issue of what are, or should be, the appropriate components of the utility's avoided costs? The Commission's decisions in various dockets have identified certain components of a utility's avoided energy and avoided capacity costs. But the Commission may undertake a comprehensive examination of what should be the full set of components that should be used in calculating the utility's avoided costs, especially in light of a broader understanding of the direct and indirect short-term, medium-term and long-term costs of using fossil fuels in Hawaii. Such a comprehensive consideration of what should constitute the components in determining the utility's avoided costs could alter the Commission's current approach to the determination of avoided costs and thus affect the ultimate impact of this statutory 100% avoided cost ceiling as it relates to potential FIT rates.

Second, HRS §269-16(a) provides, among other matters, that all rates charged by electric utilities shall be just and reasonable and shall be approved by the Commission. If the FIT rates exceed the utility's avoided costs and, as a result, the utility seeks to set its rates to be charged to the utility's customers at a higher rate than it would have charged but for the FIT rates, then the Commission must determine if such increased rates that the utility proposes to charge its customers would be just and reasonable under the Commission's statutory and regulatory criteria.

b) Does HRS § 269-27.2 create a ceiling on the feed-in tariff price?

RESPONSE:

See Response to Question 1.a) above.

c) If so, how do the signatories to the Energy Agreement (or other parties to this proceeding) propose to demonstrate that each feed-in tariff price does not violate the statute?

RESPONSE:

Based on the foregoing analysis, there appear to be two options available:

First, HRS §269-27.2 could be amended to provide that the 100% avoided cost limitation shall not apply to rates for purchase under any FIT established and approved by the Commission that requires electric utilities to purchase energy through the FIT mechanism as long as the FIT continued to promote and fulfil the objectives for the FIT set forth in the Energy Agreement. Such amendment could also include specific provisions regarding the amount of energy that could be supplied through the FIT from any one producer and similar parameters which would establish, at least indirectly, certain limits on the costs incurred by the purchasing utility that it would seek to recover from its rates charged to its customers.

Second, the Commission could re-examine what should be the elements comprising the utility's avoided costs and how should those costs be determined, taking into account those factors, among other relevant factors, listed above. This could result of determinations of avoided cost that would be conducive to potential FIT rates.

2. As with any administrative agency decision, a Commission decision approving a feed-in tariff must be supported with substantial evidence.

   a) Focusing on the price term, what evidence is legally necessary? Consider these options, among others:

      i) evidence of actual costs to develop similar project in Hawaii

ii) generic (i.e., non-Hawaii) evidence of costs associated with each particular technology

iii) evidence that the tariff price results in costs equal to or below the utility's avoided cost

RESPONSE:

On a preliminary basis, it would appear that all types of evidence listed above would be relevant, although the degree of relevance would depend in part on (i) what specific technologies would be incorporated into the FIT, (ii) what size limitations, if any, would be placed on the generator facilities that would be allowed to sell into the FIT, (iii) what volume limitations, if any, would be imposed on the amount of energy that a particular seller could sell into the FIT, and (iv) similar types of characteristics and requirements to be incorporated into the FIT mechanism. Once these are determined, at least initially (as has been proposed in the Joint Proposal on Feed-in Tariffs of the HECO Companies and Consumer Advocate, filed on December 23, 2008, in Docket No. 2008-0273 (the "Joint Proposal")), then the specific types of evidence that would be relevant could be more readily and specifically identified.

More generally, the standard for determining what evidence would be material and relevant to determine the issues involved would appear to be the same general standards as in other Commission proceedings involving determining the reasonableness of rate increases, tariffs generally, and similar proceedings.

b) By what process do the signatories (and other parties to this proceeding) propose to gather this evidence and present it the Commission, under the procedural schedule proposed by the signatories?

RESPONSE:

First Wind can only speak for itself, and proposes to respond as best as it can to the questions listed in Appendices A and C to the Scoping Paper as directed by the Commission. First Wind does note, however, that the Appendix A and C questions are much more generic and unlimited than the FIT proposal outlined in the Joint Proposal, and this raises the issue of whether First Wind's responses to the Appendix A and C questions will be relevant to the issues related to the Joint Proposal if the Commission seeks to center its focus on the Joint Proposal. First Wind also notes that the proposed procedural schedule is a very ambitious one, the specific issues related to FITs and the Joint Proposal are still to be identified, and it may be difficult for parties to assemble the evidence that will ultimately be deemed material and relevant in this proceeding within the proposed schedule.

3. Assume the Commission does create feed-in tariffs, which entitle the seller to sell to the utility at the tariff price.

a) If the tariff price exceeds the utility's avoided cost, is there a violation of PURPA, provided the seller is relying on a state law right to sell rather than a PURPA right to sell?

RESPONSE:

PURPA § 210(a) requires the Federal Energy Regulatory Commission ("FERC") to prescribe rules to encourage cogeneration and small power production, including, among other things, requiring electric utilties to offer to purchase electric energy from qualifying cogeneration facilities and qualifying small power production facilities ("QFs"). Such rules shall ensure that rates for such purchase shall be just and reasonable to the electric utility consumers and in the public interest, shall not discriminate against QFs, and shall not exceed the utility's avoided costs. PURPA § 210(b). PURPA § 210(f) requires each state regulatory authority to implement these rules. FERC has promulgated regulations pursuant to PURPA ("FERC Regulations"), 18 CFR Part 292, which contain these same provisions regarding rates for purchase. 18 CFR §292.304(a)(2). The Commission has implemented PURPA § 210(f) by promulgating its Standards for Small Power Production and Cogeneration, HAR Title 6, Chapter 74 ("PUC Standards"), which also contain substantially the same rate for purchase provisions as in the FERC Regulations.[1]

PURPA created a legal regime to deal with a national energy crisis in part by seeking encourage small power production and cogeneration, increase the use of nonfossil fuel sources of energy, and reduce the Nation's dependence on foreign oil. QFs are expressly created by PURPA, which defines what facilities constitute QFs, what rights QFs have, what obligations electric utilities have with respect to QFs, and what rates electric utilties would be required to pay to QFs for QF power. It is well-settled that "states cannot, consistent with the express language of PURPA and [FERC's] regulations, require rates that exceed avoided cost for QF sales at wholesale." *Connecticut Light & Power Company*, 71 FERC ¶ 61, 305 at 61,151, 1995 WL 216783 (FERC) (April 12, 1995); see, also, *Id.*, 70 FERC ¶ 61,012, 1995 WL 9931 (FERC) (January 11, 1995). Hence, if (i) the Commission (or the State) sets FIT rates that are higher than the utility's avoided cost, (ii) the seller, if it chose to sell under the FIT mechanism, is required to sell at the applicable FIT rate, (iii) the utility is required to purchase such power at the applicable FIT rate, and (iv) the seller is a QF as defined by PURPA, the FERC Regulations and the PUC Standards, then such FIT rate for purchase would arguably violate PURPA, and PURPA would preempt State law, including HRS § 269-27.2.

However, the FERC Regulations, in Subpart C that governs arrangements between electric utilties and QFs under PURPA § 210, states in pertinent part that the FERC Regulations in Subpart C do not limit the authority of any electric utility or QF to agree to a rate for any purchase, or terms or conditions relating to any purchase, which differ from the rate or terms and conditions that would otherwise be required under Subpart C. 18 CFR § 292.301(b). FERC itself explained that PURPA § 210 applies only

[1] §6-74-22(a)(3) of the PUC Standards provides that such rate for purchase shall not be less than one hundred percent of the utility's avoided costs and not less than the minimum purchase rate.

if a QF chooses to avail itself of the rights and protections set forth in PURPA § 210. *See*, FERC, *Final Rule on Small Power Production and Cogeneration Facilities; Regulations Implementing Section 210 of the Public Utility Regulatory Policies Act of 1978*, 45 Fed. Reg. 12214, 21217 (Feb. 25, 2980). PURPA provides a specific certification process by which QFs may be certified as such, which then entitles them to pursue their rights vis-à-vis electric utilties under PURPA § 210. *See,* PURPA § 201 *et seq.*, 18 CFR § 292.201 *et seq.* Hence, a facility that is, by definition, a QF under PURPA, may choose to avail itself of its rights under PURPA in seeking an arrangement to sell its power to an electric utility, or may choose, without availing itself of its PURPA rights, to negotiate such a purchase arrangement with a willing utility. This approach may provide a legal basis for an FIT mechanism that would be available to nonfossil fuel producers (which would likely also be QFs under PURPA) and that would offer rates for purchase above the utility's avoided costs. An issue here would be whether the exception for negotiated rates or terms under § 292.301(b) of the FERC Regulations is intended to apply only to individual case-by-case QF-utility purchase arrangements, or whether it would also apply to a Commission-approved FIT rate structure that includes rates above the utility's avoided costs and that, once approved, has general legal applicability to all sellers desiring to sell to the utility under the FIT mechanism. Nonetheless, there would also remain the waiver option discussed below.

It should be noted that the FERC Regulations provide that any state regulatory authority (with respect to any electric utility over which it has ratemaking authority) may, after public notice in the utility's service area, apply to the FERC for a waiver from the application of any of the requirements of Subpart C of the FERC Regulations, including the provisions for rates for purchase. 18 CFR § 292.402(a). Thus, if there remains a substantial legal uncertainty as described above, then the Commission could consider applying to FERC for a waiver from the avoided cost limitation to the extent necessary to allow the State to adopt and implement an FIT mechanism.

Finally, it should also be noted that HRS § 269-27.2 does not define "nonfossil fuel" nor nonfossil fuel producer or generator. However, PURPA's definition of a qualifying small power production facility (which is likely what most producers of electric energy would be which would sell energy into the FIT) would probably encompass most such "nonfossil fuel" producers. Aside from any size requirements, most QFs would have its primary energy source any one of biomass, waste, renewable resources, geothermal resources, or any combination thereof, and 75% or more to the total energy input would be from thee sources, as required by 18 CFR § 292.204, and would by definition be deemed to be "nonfossil fuel" producers. Hence, HRS § 269-27.2 would not provide a legally sustainable alternate basis in this instance, unless it is authoritatively determined that the above exception under 18 CFR § 292.301(b) is applicable to the instant situation.

b) If the tariff price exceeds the utility's avoided cost (as calculated prior to the existence of the tariff), could a seller assert a PURPA right to a sale at the tariff price, on the grounds that the utility now has a new "avoided cost" equal to cost it would have incurred under the state-mandated feed-in tariff?

RESPONSE:

It is very doubtful that a seller, whether a QF or a "nonfossil fuel" producer, could effectively make such a claim. Under PURPA, the avoided cost is defined as "the incremental costs to an electric utility of electric energy or capacity or both which, but for the purchase from the qualifying facility or qualifying faculties, such utility would generate *itself or purchase from another source.*" *18 CFR § 292.101(b)(6). Under* PURPA and the PUC Standards, the utility's customers would be neutral with respect to the cost they would incur whether the utility generated that power itself or purchased from another source. Hence, it is the utility's avoided costs, and not a higher FIT rate that is imposed upon the utility from a statutory or regulatory mandate, that would be the basis for a rate for purchase from a QF under PURPA and the FERC Regulations and the PUC Standards.

c) If the price associated with a feed-in tariff is less than the utility's avoided cost, what benefit does the tariff offer the developer that is not already available under PURPA?

RESPONSE:

The considerations that a developer, presumably a QF, would like consider in determining whether or not to invest in developing a generation facility to sell electric energy to the utility through an FIT mechanism would not necessarily be limited to the price for such energy. Depending upon how great is the difference between the utility's avoided cost and the FIT rate, the seller could find the following factors, among others, to be very relevant in making its development decision: (i) the certainty of the FIT rate and its duration, (ii) the minimum, or insignificant, difficulties of interconnection, (iii) the ability to sell its energy without need for complex and likely protracted power purchases agreement negotiations, (iv) the lesser overall development costs, (v) the relatively shorter development time, and (vi) other related development, financing, etc. factors.

Nonetheless, these factors would likely vary over time, differ for different technologies involved, influence the development objectives of each potential developer, affect project financing options, and involve similar and other considerations.

d) Please offer any other comments concerning the legal and practical relationship between the feed-in tariff and existing PURPA rights and obligations.

RESPONSE:

At this point, based on the foregoing analysis, there appear to be certain legal constraints to establishing an FIT mechanism that would set prices to be paid for electric energy supplied by QFs as defined under PURPA (including producers of electric energy generated from nonfossil fuels under HRS § 269-27.2) at rates higher than the utility's avoided costs, although the precise elements of an FIT mechanism remain to be determined. Nonetheless, possible options that might be available to facilitate the establishment of an FIT mechanism (including a mechanism as proposed in the Joint Proposal) include the following:

1. Re-examine the definition of "avoided cost" under PURPA as well as the PUC Standards to determine if, in light of all relevant circumstances, including evolving concepts of direct and indirect costs involved in electric energy generation from fossil fuels, additional components could or should be included within the definition and calculation of avoided costs.

2. Amend HRS § 269-27.2 to provide that the 100% avoided cost ceiling limitation shall not apply to rates for purchase under any FIT established and approved by the Commission that requires electric utilities to purchase energy through the FIT mechanism as long as the FIT continued to promote and fulfil the objectives for the FIT set forth in the Energy Agreement. Such amendment could also include specific provisions regarding the amount of energy that could be supplied through the FIT from any one producer and similar limiting parameters which would establish, at least indirectly, certain limits on the costs incurred by the purchasing utility that it would seek to recover from its rates charged to its customers.

3. Apply, pursuant to 18 CFR § 292.402(a), to FERC for a limited waiver from the avoided cost limitation under 18 CFR § 292.304(a)(2) to the extent necessary to allow implementation of the FIT mechanism. A basic element of the rationale for a waiver could be that the FIT mechanism would strongly and effectively promote the basic objectives of PURPA in the Hawaii context.

Respectfully submitted:

DATED: Honolulu, Hawaii, January 12, 2009.

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I hereby certify that I have this date served copies of the foregoing motion upon the following parties, by causing copies hereof to be hand delivered or electronically transmitted to each such party as follows:

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